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ABSTRACT

This paper isolates critical rural economic development issues and identifies needed federal policy interventions. Despite a long history of federal efforts to improve rural economic conditions, recent policies and programs aimed at stimulating rural development have had little impact. Reasons include: (1) narrowly focused economic development policy that fails to recognize fundamental changes in the rural economy; (2) old and inappropriate business support infrastructure; (3) inadequate human resource base; and (4) dependence on capital sources that are inadequate to meet the changing needs of rural businesses. Federal intervention to increase income and emloyment in rural America is justified on two primary bases: (1) benefits of rural economic development programs are dispersed widely across the nation and are likely to go unfunded without federal partnership; and (2) policy coordination can reduce economic waste resulting from competition between states. Future federal policy should: (1) provide financial support for educational and technical assistance programs that enhance production and entrepreneurial skills, management capacity, and leadership abilities of rural residents; (2) expand both the eligibility for and focus of current programs; (3) support development of appropriate business support infrastructure; and (4) improve rural access to development capital for businesses. Formation and implementation of effective rural development policies requires a committed partnership among federal, state, and local governments. (SV)

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INCOME AND EMPLOYMENT POLICY

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Economic problems are pervasive in rural America, and limited job prospects are causing people to leave in search of better economic opportunities. The purpose of this paper is to isolate the most critical rural economic development issues facing the nation and then identify the most needed federal policy interventions.

HISTORY OF FEDERAL RURAL INCOME AND EMPLOYMENT POLICY

Federal programs to improve economic conditions in rural communities have a considerable history in public policy. During the 1930s, for example, programs launched under the New Deal attempted to revitalize the struggling rural farm sector. New Deal Programs administered by the Farm Security Administration provided loans to poor farmers to enable them to purchase and maintain their farms. The Farmers Home Administration created during the same era made available low-interest loans to farmers unable to obtain credit through private sources.

Beginning in the 1950s federal rural economic development programs took a broader focus and attempted to encourage the location of industry in rural America through providing low-interest loans, key public facilities, training, and planning assistance. The Economic Development Administration, for example, was established in the 1960s to provide assistance for public facilities projects, job training, business loans, planning grants, and research and technical services in multi-county districts and regions. The Small Business Administration was formed to provide financial and technical assistance to smaller enterprises. While these programs were national in scope benefiting both urban and rural communities, they played an important role in encouraging manufacturing facilities to locate in rural regions.

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More recently, the Rural Development Act of 1972 established a variety of programs as well as research to provide for improving the economy in rural America. A main thrust of the legislation was toward creating jobs and stimulating business income in rural areas through loans and credit for rural industrialization. However, interest in funding programs outlined in the 1972 Act diminished throughout the 70s with improving economic conditions in rural communities.

CURRENT STATUS OF THE RURAL ECONOMY

Once again economic problems in rural America have gained the attention of policy-makers. Recent studies such as those undertaken by the Federal Reserve Bank of Kansas City and the Economic Research Service of the U.S. Department of Agriculture have documented existence of a wide range of economic problems in the hinterlands.

Table 1 provides a comparison of employment growth and unemployment rates in metropolitan and nonmetropolitan counties of each of the four major regions of the United States during the first half of the 1980s. While the national economy continues to improve, the data clearly illustrates a widening gap between economic conditions in rural counties compared to their urban counterparts.

CRITICAL RURAL ECONOMIC DEVELOPMENT ISSUES

Despite past national attention, policies and programs aimed at stimulating economic development in rural areas have fallen short of their mark. Reasons cited by policy analysts include the following:

- Failure of rural economic development policy to recognize fundamental changes in the rural economy.
- Old and inappropriate business support infrastructure.
- An inadequate human resource base.
- Dependence upon capital sources which may be inadequate for the changing needs of rural businesses.

Table 1. Employment growth and unemployment rate, 1979, 1982 and 1984.

Area and Type of Country	Percent Employment Change 1979-82	Percent Employment Change 1982-84	Percent Unemployment Rate 1979	Percent Unemployment Rate 1982	Percent Unemployment Rate 1984
UNITED STATES:					
Metropolitan	1.2%	5.9%	5.7%	9.3%	7.1%
Nonmetropolitan	-0.6	3.3	6.1	11.1	9.1
NORTHEAST:					
Metropolitan	-0.6	4.7	6.6	8.8	6.7
Nonmetropolitan	-1.8	4.2	7.0	10.6	8.1
MIDWEST:					
Metropolitan	-4.7	4.7	5.5	11.2	8.2
Nonmetropolitan	-3.9	1.8	5.5	10.8	8.9
SOUTH:					
Metropolitan	5.3	7.4	5.0	8.1	6.4
Nonmetropolitan	0.1	4.1	6.1	11.1	9.3
WEST:					
Metropolitan	4.4	6.4	5.8	9.4	7.2
Nonmetropolitan	3.3	3.7	7.3	12.0	9.8

Source: Herman Bluestone and John Hession, "Patterns of Change in the Nonmetro and Metro Labor Force Since 1979." In *New Dimensions in Rural Policy: Building Upon Our Heritage*, Joint Economic Committee, Congress of the United States, Washington, D.C., 1986.

An understanding of each of these issues is a necessary foundation for discussion of effective policy options for improving economic conditions in rural America.

Narrowly Focused Policies and Programs

Historically, rural economic development policies and programs have focused narrowly on agriculture and extractive sectors of the economy and on attracting manufacturing industries to rural communities. Of major note is that eligibility requirements for state and federal grants, loans, and technical assistance typically exclude retail and service producing businesses. Public assistance for site development, planning, and training efforts in rural communities typically focuses on manufacturing rather than on emerging growth areas in health care, retirement industries, residential development or main street businesses.

The traditional narrow focus of rural economic development policy preserves the existing economic structure in rural communities and tends to undermine the dynamic evolution necessary to maintain rural economic vitality. Healthy economies are dynamic allowing enterprises for which there are declining market opportunities to be replaced by emerging new economic opportunities. In today's economy, many of those opportunities are outside of agriculture, mineral industries and manufacturing.

A second major disadvantage of the current narrowly focused programs is that they do not impact a broad spectrum of rural communities. For example, policies focused on locating manufacturing in rural areas are of little value to the numerous smaller, isolated rural communities with limited manufacturing development potential. Strategies such as tourism and recreation development, tapping the communities potential as a residential or retirement center, or development of local home-based businesses are often more appropriate than attempts to attract manufacturing to rural communities.

Old and Inappropriate Infrastructure

Much concern has been raised in recent years over the availability and quality of business support infrastructure in rural America. For example, many of the roads and

bridges constructed during the first part of this century were engineered for smaller vehicles than the large tractor-trailer trucks which carry products to and from rural communities today. Water and waste disposal systems are in disrepair or out-of-date in many rural communities. This places a great burden on rural communities by causing expensive repairs and making them unattractive areas for new businesses to locate.

The concern extends beyond traditional infrastructure investments such as highways or sewer and water facilities to include emerging new infrastructure needs. Telecommunication facilities are an example of an emerging new infrastructure need in rural America and an increasingly important support facility for American enterprise. Private telecommunication firms often find it unprofitable to invest in rural areas due to the sparse population base. Rural communities lacking access to key telecommunication technologies will be at a competitive disadvantage in attracting and retaining business and industry.

Sparsely populated rural communities are at a particular disadvantage in financing necessary public facilities and services due to their limited taxing capacity. In many cases, their local taxing capacity has been further eroded in recent years by declines in property values resulting from declines in agriculture, manufacturing and natural resource based industries. A problem of particular concern is the real possibility that rural communities most in need of new investments in business support infrastructure as a means to accommodate a restructuring of their local economy may be the least able to afford such investments.

Lack of an Adequate Human Resource Base

An entire paper in this series is devoted to rural education and training. Education and training is critical to the development of a productive labor force in rural America. A productive labor force in turn is critical to the future competitiveness of rural business and industry.

Human resource development programs supporting rural economic development must go beyond traditional education and skill training. In particular, effective management and

entrepreneurship skills are vitally needed by rural residents participating in the economy of the future. The selective out-migration from rural areas has resulted in a shortage of business leaders skilled in the techniques necessary to cope with the difficult and changing rural economy. The relatively small size of rural firms and the preponderance of sole proprietorships have resulted in businesses being managed by single individuals rather than the departments of specialists which characterize the larger urban corporations. The smaller size markets often mean that the necessary specialized business services are not available even on a consulting basis. Business schools and the services of the Small Business Administration and community colleges are not as readily available in rural areas.

Development of public management and community leadership skills among rural residents is equally as critical for the development and implementation of effective economic development efforts in rural America. While urban communities typically maintain a professional staff to oversee local economic development planning efforts, most rural communities rely on volunteer leaders and part-time staff. The changing economic environment in combination with recent policies shifting additional responsibilities for economic development planning to the state and local levels has increased the need for strong economic development leadership in rural areas.

Capital Sources Which May Be Inadequate

Rural financial institutions have experienced a crisis stemming from the agricultural crisis of the 1980s and the precipitous drop in mineral, timber, and energy prices. Those institutions with portfolios that have included a high proportion of agriculture and natural resource based loans have experienced severe liquidity problems. Cash flow from these industries has been inadequate to service debt, and collateral values have dropped precipitously, making debt restructuring impossible in many situations. This credit crisis and the resulting liquidity problems of rural financial institutions may limit credit availability for important future business and economic development projects.

There remains concern that large nonlocally owned banks may be less responsive to the

credit needs of rural farmers and entrepreneurs than locally owned banks. A similar problem associated with the increased concentration of business assets has also been noted. A small scale local entrepreneur is more likely to reinvest in local enterprises in the community while a large nonlocal corporation has a greater tendency to respond to opportunities in other locations. A heavy reliance on outside investment capital may be partially responsible for employment instability in rural areas.

JUSTIFICATION FOR FEDERAL ROLE

Economic conditions in rural America have continued to lag behind urban places throughout this decade. The gap between rural and urban economies is likely to grow even wider without significant federal policy intervention to address key issues such as the need to encourage economic diversification, to update old and inappropriate business support infrastructure, to educate and retrain inadequate human resources, and to assure the availability of capital in rural communities.

Clearly, successful programs addressing the critical rural economic development needs require active involvement of state and local governments. However, state and local resources are generally inadequate to deal with the extensive problems facing rural America. Federal intervention to aid in increasing income and employment can be justified on two primary bases:

- The benefits of many rural economic development programs are dispersed widely across the nation. For example, benefits from a program to improve management skills of rural business people are lost from the rural community or state as business people trained under the program move to another location. Without a federal partnership, programs such as these are likely to go unfunded as state and local governments do not have a clear incentive to fund programs for which their constituencies are unable to capture the full benefits.
- Coordination of rural economic development policy can also help reduce economic waste resulting from competition between states. Public tax receipts are diminished

in all states as states provide tax incentives and "give away" programs to attract business and industry. The net impact on business location decisions is minimal as competing states offer about the same incentive packages. Only strong coordination at the federal level can overcome the problem of wasteful competition between states.

FEDERAL INCOME AND EMPLOYMENT POLICY OPTIONS

Federal rural economic development policy intervention options addressing the changing needs of rural America include four broad categories:

- Providing financial support for educational and technical assistance programs enhancing production and entrepreneurship skills, management capacity, and leadership abilities of rural residents.
- Expanding eligibility requirements and focus of rural economic development programs to support a broader range of business and industrial development opportunities than are supported by present programs.
- Providing financial support to aid communities in developing an appropriate mix of business support infrastructure.
- Utilizing federal regulatory powers and direct financial assistance to ensure entrepreneurs access to adequate capital for starts and expansions of rural enterprises.

A brief analysis of the potential beneficial impacts of each of these policy intervention options for rural economies is provided below.

Broaden Focus of Current Rural Economic Development Programs

Effective rural economic development policy must recognize the diverse needs of rural communities by supporting a broad range of economic development opportunities. These opportunities extend beyond the traditional farm policy and industrial recruitment and could be supported through broadening the focus of federal programs. Specific examples include but are not necessarily restricted to the following: targeting federal procurement dollars for

businesses in rural areas; identifying and developing foreign markets for rural-based businesses; providing tax incentives, grants and loans to stimulate development of new retail and service businesses in rural business districts; supporting research to develop new products and markets from resources available in rural areas; and broadening eligibility requirements of economic development programs to include export-oriented service businesses.

Expanding the focus of rural economic development programs will encourage the diversification of rural economies into emerging growth opportunities and will result in federal assistance reaching a broader range of communities than are helped by present federal programs.

Provide Financial Support for Development of Appropriate Business Infrastructure

The federal government has traditionally played a major role in financing key infrastructure facilities and services in rural areas including highways, roads, bridges, sewer and water facilities, and industrial sites. As noted earlier, there is a need to expand the federal role to include emerging new business-support services such as telecommunication facilities.

Facilities and services such as these are necessary but are not sufficient by themselves to promote rural economic development. A wide variety of other factors are equally important, including access to markets and key inputs, availability of labor with needed skills, availability of capital, and effective community leadership. If other key factors of production are not in place, construction of highways, sewer and water facilities, or industrial sites will do little good. On the other hand, when other factors necessary for economic success are present, an inadequate infrastructure base can seriously hamper economic development.

Due to the costly nature of infrastructure facilities and the fact that the benefits of such infrastructure extend beyond the rural area, federal assistance is needed to help rural communities make the necessary infrastructure investments to support rural economic development. Discussion of specific policy options is deferred to a companion paper in this

series addressing policy considerations for the finance of rural public facilities and services.

Provide Financial Support For Rural Human Resource Development

Human resources are the key to a strong rural economy. Rural businesses require a productive labor force. Business management and entrepreneurship skills play an important role in supporting the start of new rural businesses as well as the retention and expansion of existing ones. Community leadership skills are necessary ingredients for effective local economic development planning.

Unfortunately, rural communities and states often lack the necessary financial resources to expand educational and technical assistance programs designed to enhance production and entrepreneurship skills, management capacity, and leadership abilities of rural residents. Furthermore, the incentive for localities and states to finance human resource development programs is limited by a recognition that the benefits of such programs are often lost from the locality or state as people move from the area. Consequently, significant inroads into solving the quality and availability of human resources in rural areas is unlikely without federal cost sharing for education and technical assistance programs.

Improve Access to Financial Capital for Starts and Expansions of Rural Enterprises

Financial assistance to rural enterprises through loans, direct grants, and tax subsidies have historically been an important part of federal policy to encourage development of business and industry in rural communities. Federal financial assistance programs administered by agencies such as the Economic Development Administration and the Small Business Administration are needed to support economically sound ideas of rural entrepreneurs unable to obtain business development capital from conventional sources. Current eligibility requirements for federal programs should be broadened to include business development opportunities in the rapidly growing service sector.

Many rural financial institutions, community development groups, and business people do not utilize available financial assistance programs simply because they are unaware of them or they find the rules and regulations too complicated. Technical assistance to both rural communities and businesses are necessary to ensure effective implementation of federal financial assistance programs.

In addition to direct financial assistance, federal regulatory powers over financial institutions can be utilized to improve access to business development capital in rural areas. For example, existing regulations need to be modified to accommodate the short run liquidity problems of small rural banks affected by economic problems in agriculture and energy industries.

NEED FOR A FEDERAL, STATE, AND LOCAL PARTNERSHIP

Federal rural economic development policies must be broad based and flexible in order to recognize the diversity that exists throughout rural America. Towards this end, active and coordinated partnership among the federal, state, and local levels of government is required.

State and local governments are better able than the federal government to identify specific economic development needs and opportunities for their rural regions. However, state and local governments typically lack the necessary resources and the incentive to finance critical rural programs. Consequently, the most important role for the federal government is that of providing financial support for key business infrastructure, strengthening the capacity of rural human resources, and filling rural credit market gaps. Without a committed partnership between federal, state, and local governments in rural economic development, significant progress in improving economic conditions in rural America is unlikely.